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National Tea Co.

Annual Report

For the Year Ending December 31, 1938

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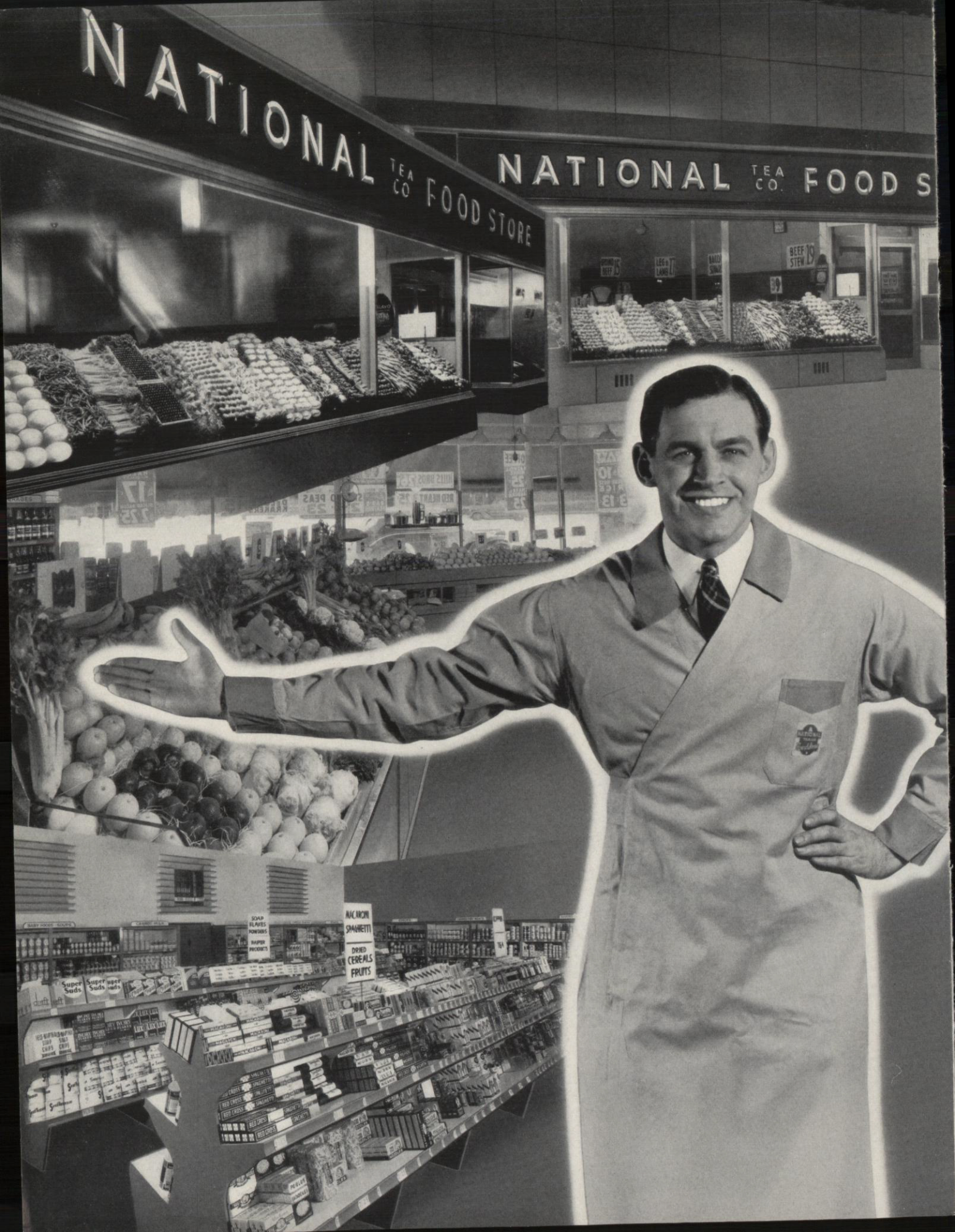
National Tea Co.

Annual Report

to the Stockholders

For the Year Ending December 31, 1938


NATIONAL TEA CO FOOD STORE
NATIONAL TEA CO. FOOD S
BEEF STEW 19
MACARONI SPAGHETTI
DRIED CEREALS FRUITS
SOAP FLAKES POWDERS PAPER PRODUCTS
Super Suds

National Tea Co.

February 24, 1939

TO OUR STOCKHOLDERS:

The results of 1938 are presented in the accompanying annual report. Disappointment and encouragement go hand in hand. We have sold less goods; we have lost less money. Our sales amounted to $55,545,216, a decrease of 10.55% from a year ago. Our net loss was $982,313, or 28% less than a year ago. In a year when most companies were working hard to retain the previous year's volume, it seemed rather our job to get things cleaned up, so that later we might go after business on a more profitable basis. A few things may be mentioned that have had our attention.

We have closed 139 unprofitable stores, while we have opened only 37 stores. This was not the result of any plan to reduce the total number, but rather shows the greater ease of deciding on stores that should be closed than of finding desirable locations for new ones. It is our intention to open new outlets wherever we think they may be profitable, in the area covered by our distributing facilities.

For many years we have been under contract to operate the food department of a Chicago department store. We have canceled that contract, which will affect our volume in 1939, but improve our profit position. The particular unit never bore any part of the National Tea Co. general overhead, and, as the business was not done in our name, there should be no loss of good will. The unit had been a steady loser for the last eight years, and did not naturally fit into our business.

Repairs and maintenance of our stores have been much neglected in recent years. What was spent was generously spent on a few stores, while most of them had little or no attention.

We have been trying hard to catch up. Last year we spent $239,000, but there is still much to be done. We estimate it will take about $200,000 more to get our stores looking as they ought to look, and this will be in addition to the normal expenditure and investments in new equipment. This item of $200,000 will naturally affect our 1939 income, as our auditors have discouraged the idea of setting aside a reserve out of surplus to take care of this item that really belongs to previous years.

For ten years this company owned an undivided half interest in the Nateco Realty Trust. The property in the Trust consisted largely of a number of pieces of real estate, in some of which we rented stores; also, shares of stock in the National Tea Co. and some notes receivable—the chief of which was one due from this company for $131,023.94. So that we might have entire control of what we owned, we surrendered our trust certificates and received one half of the assets of the Trust in exchange. Our half consisted of certain land and buildings, 5,600 shares of our common stock, 50 shares of our preferred stock, a secured note of one of our officers for $12,500, and a reduction of our Nateco note liability by $100,105.34.

The present policy of this company is to rent its store locations rather than own them. In pursuance of this policy, it is our intention to sell the properties which we at present own. During the year, because of the unfavorable condition of the real estate market, we sold only three pieces, for a total of $36,000. We have many other properties which we shall gladly sell, and in many cases we shall be willing to rent stores back from the new owners.

A number of years ago the company sold some of its preferred stock to certain employees, including officers, on a plan of extended payment. The plan did not work out well and was the cause of dissatisfaction on the part of the employees. At our suggestion, the contracts (excepting those of officers) were surrendered, shares of stock to the amount paid for at the price originally agreed upon were given to the employees, and the balance canceled. To have continued the scheme would have been detrimental to the business, and the settlement of the question was an act of justice and produced a much better feeling among all those concerned. The $26,499 appearing on the balance sheet covers the officers' contracts only, and it is our intention to consider this problem in 1939.

A number of changes in department heads have been made, and bid fair to be very helpful. We were glad to be able to do this without going outside our own personnel.

We have dissolved nine of the subsidiaries referred to a year ago. Those that remain are wholly owned by the company and present no embarrassment.

Commitments for merchandise beyond our current needs are not in excess of $100,000.

Our gross profits are now showing a substantial improvement, although prices have not been raised, but rather lowered. The improvement has been brought about by more skilful merchandising and elimination of waste.

Our earnings by quarters have been published, but that our stockholders may see the whole picture, we compare the net results for the two years, as follows:

	1938	1937
First quarter	*$207,097* Loss	$ 109,828 Profit
Second quarter	*176,341* Loss	*100,355* Loss
Third quarter	*444,816* Loss	*846,637* Loss
Fourth quarter	*154,059* Loss	*528,116* Loss
Year	*$982,313* Loss	*$1,365,280* Loss

As to the future, we would rather not make any predictions. But, because the management was able to reduce inventories, we have a little more money on hand and a million dollars less debts, and, with a heightened morale throughout our organization, the future looks better than it did a year ago.

Your chairman takes this opportunity to express his personal appreciation for the wholehearted and loyal co-operation given by the entire organization, from the officers to the most recently hired clerk.

By order of the Board of Directors,

John McKinlay

CHAIRMAN

Consolidated

DECEMBER 31,

ASSETS

	1938	1937
CURRENT ASSETS:		
Cash on hand and in banks	$ 1,354,251.24	$ 1,273,686.00
Notes receivable—		
Officer (secured by 4,500 shares National Tea Co. preferred stock)	$ 12,500.00	—
Others (less reserve for doubtful notes)	1,236.25	$ 18,262.27
	$ 13,736.25	$ 18,262.27
Accounts receivable—		
Trade	$ 241,588.42	$ 236,496.57
Due from relief agencies	166,607.77	155,478.21
Due from employes for cars purchased from company	17,905.91	—
Other receivables and deposits	43,089.05	68,412.52
	$ 469,191.15	$ 460,387.30
Less: Reserve for bad debts	67,787.20	33,854.11
	$ 401,403.95	$ 426,533.19
Inventories of merchandise and supplies in company and outside warehouses certified as to quantities and condition by officials of the company and valued at cost or market, whichever is lower	$ 3,929,349.33	$ 5,203,720.76
Total current assets	$ 5,698,740.77	$ 6,922,202.22
EMPLOYES' STOCK SUBSCRIPTION CONTRACTS:		
Investment in contracts for sale of preferred stock of National Tea Co. and secured by such stock (unpaid balances of contracts, except those of officers were cancelled on August 26, 1938 and the 2,073 shares of stock released by the cancellations were acquired for the treasury)	$ 26,499.46	$ 50,815.69
MORTGAGES AND NOTES RECEIVABLE	$ 19,245.88	$ 16,183.29
INVESTMENTS:		
Nateco Realty Trust—represented by 500 certificates of beneficial interest, being 50% ownership at cost (surrendered December 31, 1938 in exchange for one-half of the assets of the Trust)	$ —	$ 668,870.51
Sundry — at cost	4,022.63	4,217.63
	$ 4,022.63	$ 673,088.14
PROPERTIES — AT COST UNLESS OTHERWISE STATED:		
Land	$ 3,448,696.16	$ 3,155,417.42
Buildings (at cost less reduction in valuation as of June 17, 1935 as determined by Board of Directors)	$ 5,119,940.05	$ 4,958,364.14
Less: Reserve for depreciation	1,677,247.71	1,531,277.10
	$ 3,442,692.34	$ 3,427,087.04
Store fixtures and equipment	$ 5,913,595.28	$ 6,283,768.80
Less: Reserve for depreciation	4,272,433.07	4,233,344.04
	$ 1,641,162.21	$ 2,050,424.76
Machinery, fixtures and equipment	$ 1,803,081.94	$ 1,835,313.03
Less: Reserve for depreciation	1,481,686.54	1,433,345.53
	$ 321,395.40	$ 401,967.50
Delivery equipment	$ 730,475.44	$ 866,412.10
Less: Reserve for depreciation	629,910.06	673,780.89
	$ 100,565.38	$ 192,631.21
Total properties	$ 8,954,511.49	$ 9,227,527.93
GOOD WILL	$ 1.00	$ 1.00
DEFERRED CHARGES:		
Prepaid rents, taxes, insurance, etc	$ 111,817.87	$ 139,200.00
	$14,814,839.10	$17,029,018.27

Balance Sheet

1938 AND 1937

LIABILITIES AND CAPITAL

			1938	1937
CURRENT LIABILITIES:				
Notes payable—				
Banks			$ 500,000.00	$ 1,400,000.00
Nateco Realty Trust			30,918.60	30,000.00
			$ 530,918.60	$ 1,430,000.00
Accounts payable—				
Trade, etc.			$ 1,285,290.74	$ 1,146,169.95
Pay roll and commissions			40,838.49	36,384.62
Interest and taxes			545,375.94	530,032.53
Employes' deposits			4,299.77	9,217.14
Provision for unjust enrichment tax			—	88,080.90
Provision for federal and social security taxes			151,099.26	188,343.97
			$ 2,026,904.20	$ 1,998,229.11
Real estate mortgage notes due within one year			$ 34,250.00	$ 70,250.00
Commercial letters of credit (merchandise received or in transit)			$ 91,837.12	$ 123,234.64
Total current liabilities			$ 2,683,909.92	$ 3,621,713.75
NOTES PAYABLE—NATECO REALTY TRUST, DUE MAY 31, 1939			$ —	$ 131,023.94
REAL ESTATE MORTGAGE NOTES, DUE AFTER ONE YEAR (includes an amount of $443,750.00 payable $6,250.00 quarterly from January 2, 1940 to April 1, 1947 and $256,250.00 on July 1, 1947)			$ 513,750.00	$ 554,250.00
RENTAL OF CLOSED STORE, PAYABLE $3,000 PER ANNUM FROM JANUARY 2, 1940 TO AUGUST 1, 1948			$ 26,000.00	$ 29,000.00
CONTINGENT RESERVE			$ 67,464.52	$ 54,811.05
CAPITAL STOCK:				
Preferred—5½% cumulative par value $10 redeemable at par on call or liquidation —	*Shares*			
Authorized and issued	200,000	200,000	$ 2,000,000.00	$ 2,000,000.00
Less: Held in treasury	54,243	52,120		
Outstanding	145,757	147,880		
Common—no par value—	*Shares*			
Authorized	800,000	800,000		
Issued	660,000	660,000	8,250,000.00	8,250,000.00
Less: Held in treasury	37,350	31,750		
Outstanding	622,650	628,250		
			$10,250,000.00	$10,250,000.00
EARNED SURPLUS:				
As per statement attached			$ 2,213,621.61	$ 3,246,934.83
Less: Capital stock held in treasury—	*Shares*			
Preferred	54,243	52,120	$ 538,998.00	$ 518,049.25
Common	37,350	31,750	400,908.95	340,666.05
			$ 939,906.95	$ 858,715.30
			$ 1,273,714.66	$ 2,388,219.53
No dividends on preferred stock have been paid since November 1, 1937. The cumulative arrears thereon to December 31, 1938 amount to $93,527.41.			$14,814,839.10	$17,029,018.27

Income and Surplus Account

FOR THE YEARS ENDED DECEMBER 31, 1938 AND 1937

	Year ended December 31	
	1938	*1937*
Sales	$55,545,216.07	$62,100,160.50
Deduct:		
Cost of sales and expenses, including sales and occupation taxes	$55,783,314.08	$62,586,759.78
Depreciation (year 1937 includes $60,000 additional charge on fixtures removed from closed stores)	787,590.80	932,830.42
	$56,570,904.88	$63,519,590.20
Net operating loss	*$ 1,025,688.81*	*$ 1,419,429.70*
Deduct:		
Dividends received from investments—		
Nateco Realty Trust	$ 25,000.00	$ 46,000.00
Sundry stocks	102.67	41.95
	$ 25,102,67	$ 46,041.95
Profit on disposal of capital assets	14,590.27	25,142.25
Refunds of processing taxes (after deducting provision for unjust enrichment tax)	11,316.45	49,931.51
	$ 51,009.39	$ 121,115.71
	$ 974,679.42	*$ 1,298,313.99*
Add:		
Additional provision for federal income tax assessment for year 1933	$ 7,633.80	
Provision for lease cancellations or rentals on closed stores		$ 64,750.35
Net loss before provision for federal income tax	*$ 982,313.22*	*$ 1,363,064.34*
Provision for federal income tax on profits of subsidiary company		2,215.62
Net loss transferred to surplus	*$ 982,313.22*	*$ 1,365,279.96*
Earned surplus at beginning of year	3,246,934.83	4,774,300.47
	$ 2,264,621.61	$ 3,409,020.51
Deduct:		
Amount paid under National Labor Relations Board award as a result of warehouse employes' strike in 1937	$ 51,000.00	
Dividends paid —		
Preferred		$ 67,848.18
Common		94,237.50
	$ 51,000.00	$ 162,085.68
Earned surplus as per balance sheet	$ 2,213,621.61	$ 3,246,934.83

Italic figures indicate Loss.

Auditor's Certificate

BOARD OF DIRECTORS,
NATIONAL TEA CO.,
CHICAGO.

We have made an examination of the consolidated balance sheet of National Tea Co. as at December 31, 1938 and of the statement of consolidated income and surplus for the year ended on that date. In connection therewith we examined or tested accounting records of the company and its wholly owned subsidiaries and obtained information and explanations from officers and employes of the companies; we also made a general review of the accounting methods and of the operating and income accounts for the year but we did not make a detailed audit of the transactions.

We previously had made a similar examination for the year ended December 31, 1937.

The assets of the Nateco Realty Trust, acquired in exchange for the investment therein, were taken over at cost to the Trust less depreciation provided by the Trust and include land, buildings and 5,600 shares of common and 50 shares of preferred stock of the National Tea Co.

In our opinion, based upon such examination, the accompanying consolidated balance sheet and related statement of income and surplus fairly present, in accordance with accepted principles of accounting consistently maintained by the companies during the year under review, the financial position of the company at December 31, 1938 and the results of its operations for the year ended that date. For the purpose of comparison there are presented also the consolidated balance sheet and related statement of consolidated profit and loss and surplus for the year 1937.

ARTHUR YOUNG & COMPANY
CERTIFIED PUBLIC ACCOUNTANTS.

Chicago, Illinois,
February 16, 1939.

National Tea Co.

DIRECTORS

Frederick H. Massmann

George Rasmussen, Jr.

John McKinlay

Robert V. Rasmussen

Joseph L. Merrill

William E. Russell

Judson F. Stone

OFFICERS

John McKinlay
Chairman

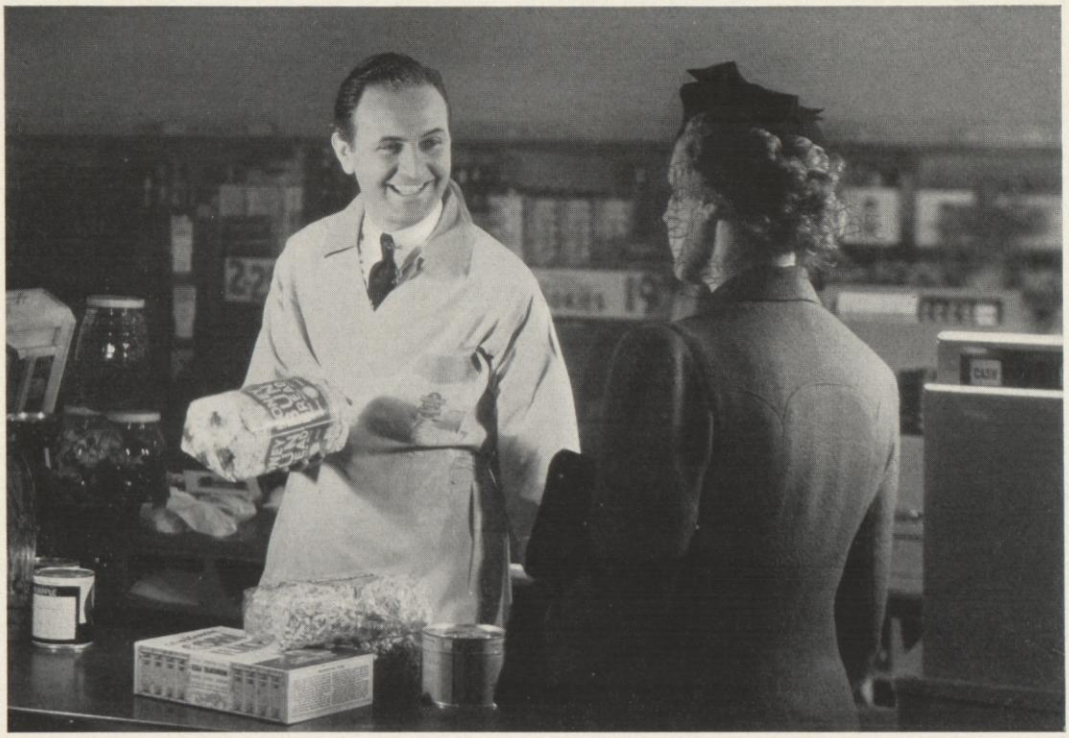
Frederick H. Massmann
President

Robert V. Rasmussen
Vice President

Burt J. Dickens
Vice President

Th. Rasmussen
Treasurer

William E. Russell
Secretary-Comptroller



New Training Course Program for Store Personnel

During 1938, store personnel control was entirely changed from district to centralized control. This change has proven many advantages.

With the ever greater need of improved sales personnel and store management, we have established a central training course program. Here clerks within our employ having managerial qualifications, are given the advantage of careful, uniform training so as to qualify them for store management.

Store managers indicating supervision qualifications, are given special supervision training. We also contemplate a uniform training course for all steady clerks.

The many advantages of these training courses are obvious. They represent one of the many improved procedures being established which are certain to react beneficially to our business.